

basis of accounting. Net income, which is essentially the difference between revenues and expenses for the period, is added to retained earnings on a periodic basis. The Income Statement's primary focus is on the entity's financial performance or profitability.

23. The Statement of Cash Flows reports the inflow and outflow of cash during the period. While the Income Statement focuses primarily on profitability, the Statement of Cash Flows primarily focuses on liquidity and solvency. Liquidity represents the ability of the entity to meet its current obligations when due, while solvency represents its ability to meet its long-term obligations. The Statement of Cash Flows provides information about a company's ability to generate cash flows in future periods, its capacity to meet obligations, its expected external financing requirements, and how successful investment and financing activities have been managed.

24. Additionally, jurisdictional entities include in the FERC Annual Report Forms a Notes to the Financial Statement schedule which provides additional explanations on the items and amounts reported in the above mentioned financial statements. The Comparative Balance Sheet, Statement of Income, the Cash Flow Statement, the Notes to the Financial Statements, and other schedules contained in the FERC Annual Reports are attested to by an officer of the company. Public utilities and licensees, and natural gas companies also file an auditor's report with the Commission certifying that the financial information contained in the FERC Annual Report Forms conform in all material respects with the requirements of Uniform Systems of Accounts and published accounting releases. In addition to collecting financial information, the FERC Annual Report Forms collect non-financial information about the operations of the entity. These reports are considered non-confidential in nature and therefore made available to the general public.

C. Relevancy of Periodic Financial Information

25. The FERC Annual Report Forms provide the Commission, as well as others, with an informative picture of the jurisdictional entities' financial condition along with other relevant data that is used by the Commission, as well as others, in making economic judgements about the entity or its industry.

26. For financial information to be useful to the Commission, as well as customers, investors and others it must be understandable, relevant, reliable,

and timely. As financial reporting has evolved over the years, users of financial data have been willing to forgo some precision in reliability for the ability to obtain the information on more timely intervals, such as on a quarterly basis.

27. Quarterly financial reporting is not a new requirement for public corporations.¹⁴ It began in 1902 when the United States Steel Corporation first published quarterly financial information and by 1910 the New York Stock Exchange added quarterly financial reporting to its listing requirements.¹⁵ Additionally, over the decades public companies have been expanding their financial disclosures to meet the needs of the user community.

28. The trend toward more frequent and better financial disclosures has increased in reaction to highly publicized corporate scandals, business failures and the resulting losses incurred by investors and others. In 2002 Congress passed the Sarbanes-Oxley Act, the most important piece of recent legislation affecting corporate governance, financial disclosure and the practice of public accounting.¹⁶ This act requires public companies to disclose on a rapid and current basis such additional information concerning material changes in the financial condition or operations in plain English for the protection of investors and the public. As a result of this legislation, dates for periodic reporting of financial information have been accelerated, and principle executive and financial officers must each attest to the validity of the financial and other information contained in the periodic reports, including information concerning off-balance sheet arrangements, contingent obligations and comments and other significant items.

29. While some jurisdictional entities may file similar information with the SEC, the level of detail concerning assets, liabilities, stockholder's equity along with the revenues, expenses, gains and losses is different for the Commission and the SEC. The financial statements filed with the SEC are on a consolidated, or parent company basis. The Commission notes that a majority of the jurisdictional entities that it

regulates file financial information with the SEC that consolidates their assets, liabilities and profits with their parent company, or combine the regulated and unregulated operations in the reports to the SEC. While consolidation is appropriate for SEC reporting, the Commission requires more detailed information concerning the results of operations, and the financial position of each jurisdictional entity in order to meet its regulatory needs. Therefore, the Commission has required jurisdictional entities to file financial information on a jurisdictional entity level basis using a uniform system of accounts.

30. Although the Commission requires jurisdictional entities to file financial information, a general weakness in this reporting program has been the frequency with which the financial reports are required. In a rapidly changing business environment, annual reporting is simply insufficient. For financial information to be useful to the Commission it must be collected on a more timely basis. In order to improve the decision making of the Commission and other users of the information, we are proposing quarterly reporting of financial and financial related information.

31. Quarterly reporting of financial information will provide the Commission, as well as customers, investors, and others with an important tool to help identify emerging trends and issues affecting jurisdictional entities within the energy industry. It will also provide timely disclosures of the impacts that new accounting standards or changes in existing standards have on jurisdictional entities, as well as the economic effects of significant transactions, events, and circumstances.

32. Furthermore, as the Commission considers implementing new accounting standards it is important that the Commission have timely financial data so that an appropriate assessment can be made of the impact these changes have on jurisdictional entities. The use of financial analytical tools and financial statements, together with the disclosures made in the notes to the financial statements and the MD&A, and other relevant data help staff, as well as, others to assess the credit quality, liquidity, solvency, and the impact that regulatory actions and economic events will have on jurisdictional entities.

33. Quarterly reporting will permit the Commission to better understand trends and other factors that may affect an entity's liquidity position, its commitments of capital expenditures, its sources of financing, along with changes in the amount and types of

¹⁴ See President's Ten-Point Plan to Improve Corporate Responsibility and Protect America's Shareholders issued on March 7, 2002. The first two points of the plan state that each investor should have quarterly access to the information needed to judge a firm's financial performance, condition, and risks. Additionally, each investor should have prompt access to critical information.

¹⁵ See Robert S. Kay and D. Gerald Searfoss, *Handbook of Accounting and Auditing* (2nd ed. 1989).

¹⁶ *Supra* Note 6.